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Banks are their own worst enemy



NOEL WHITTAKER

THE big banks have been all over the news this week, and for all the wrong reasons.

First, it was ANZ locking horns with ASIC over alleged manipulation of interest rates. Next it was the Commonwealth Bank, who got a bucketing on *Four Corners* last Monday night for unethical and unscrupulous behaviour towards claims on their insurance division, CommInsure. And last Monday ANZ bank stepped into the limelight again, revealing that it had been hit with a \$212,500 penalty for breaching responsible lending laws when offering overdrafts.

Despite the predictable protests from the banks, there is nothing new in this. In 2001, ex-bank executive Graham Hand published his best-seller *Naked Among Cannibals*, which contained more than 300 pages about corporate greed and unethical behaviour by Australian banks.

According to mortgage broker Peter Cooper, there are other areas where the banks need to be more transparent. An area of particular interest to him is fixed interest rates on loans.

As Cooper points out, a person who applies for a fixed-rate loan has the option of accepting whatever rate the bank wants to offer on the day of settlement, or paying a special fee to lock in the rate. This fee can be a percentage of the loan amount, or a fixed fee, depending on the lender.

Borrowers tend to prefer paying the fee, in one form or another, rather than take a punt on what the bank may charge them on date of settlement. Potential problems arise when the borrower needs to pay out the loan early. According to Cooper their first port of call will usually be the



TRUE STORY: Graham Hand has shone a light on corporate greed and unethical behaviour by banks.

bank, to find out how much the break costs will be. The reply from the staff member will almost certainly be that they will need to check with the bank's Treasury Department who will calculate the number.

The borrower may well get a shock when the break fee is finally advised to them, but when they query it, they may be given a work sheet that even an actuary would have a hard time understanding. Any further queries may be met with the suggestion to check the terms and conditions booklet they were given when the loan was taken out. The borrower is completely at the mercy of the bank's Treasury Department.

Apparently, when a bank makes a fixed-rate loan, that individual loan is bundled with many other loans, and placed by the bank with an outside source at a set fee. This fee is referred to as the funding cost. In order to cal-

culate the break fee, only four pieces of information are necessary. They are the funding cost, the remaining term of the loan, the balance outstanding and the funding cost when the loan is discharged. The first is almost impossible to find out, because the bank keeps the information confidential, while the other three are simple to work out.

Cooper believes – in the interests of transparency, and to protect both the bank and the borrower from conflict in the future – the bank should advise the borrower what the initial funding cost is when they issue the breakdown of settlement proceeds letter around a week after the loan is settled. Then it would be a simple matter for the borrower or their advisors to calculate the break cost if they were considering exiting the loan early.

Neither Cooper nor I are suggest-

ing that the banks are manipulating break fees for their own profitability, even though the behaviours of their treasury departments are under scrutiny right now. There have been many instances where borrowers have been stunned by the size of the break costs, and by the bank's inability to explain the reasoning behind them. The idea of advising initial funding costs at the time the original loan is settled is a good one, and simple to put into practice. It would also enable the banks to be more transparent and prevent further bad publicity. Surely that is in everyone's interest.

Noel Whittaker is the author of *Making Money Made Simple* and numerous other books on personal finance. His advice is general in nature and readers should seek their own professional advice before making any financial decisions. Email: noel@noelwhittaker.com.au

The Mario and Janet Show an unfolding drama



TERRY MCCRANN

THANKS a million Mario, Reserve Bank governor Glenn Stevens would probably have muttered Friday, as he watched the Aussie dollar jump through US75¢.

He now has to hope that Janet will surprise the world next week with an official US interest rate *increase* – something that has been made directly *less* likely as a result of

Mario's move. Mario is the poker-faced head of the European Central Bank, Mario Draghi. There was no surprise in the ECB's decision Thursday night Australian time, to cut its key rates, moving one of them even further *negative*.

The surprise was the decision to also dramatically increase its quantitative easing program (read money printing).

The impact is likely to further weaken the euro, as it becomes even less attractive for global money managers to hold them. If the euro weakens, the US dollar goes higher.

So if Janet – Janet Yellen, the head of the US Federal Re-

serve – raised the US rate, it would likely put a rocket under the greenback.

It was already unlikely that the Fed was going to hike in March – precisely because of these “currency wars”; the ECB move probably now locks that in cement.

Further it probably pushes back even deeper into the year the timing of the Fed's next rate rise, if indeed it doesn't eliminate it entirely.

Stevens is one of the people caught in the middle of this cross-Atlantic rate and currency arm-wrestle. The Aussie dollar immediately popped through US75¢. Then over-

night Friday is pushed to nearly US76¢.

While this might be good news to someone planning an overseas trip, it's less than great news for the economy. We need a lower dollar to encourage Australian businesses to invest and create jobs.

Our problem is that our interest rates are just “too high”. And that's sucking in some of the trillions of dollars sloshing around in global markets looking for some sort of return.

Now the RBA might have signalled a greater willingness to cut its official rate. Previously it had said our inflation may allow it to cut; in its latest

statement a fortnight ago it said the inflation *would* allow it to cut.

The ECB and the Fed – and the Bank of Japan – show exactly the mess you end up in when you do cut your official rate all the way to zero. Stevens would prefer not to go there.

More broadly, we can all “thank” Mario for almost certainly unleashing more volatility on global markets.

We got a taste of that in Europe Thursday and Friday. Initially after his announcement European share markets rocketed higher. Why not? He'd just poured fuel into them.

Then they suddenly re-

versed course, giving up all their gains and going sharply negative. Why? Because at his conference he said: “That's it.” There'll be no more.

But next day, the bulls were back. The European markets and Wall St rocketed up again.

Why? Because investors realised that even if the ECB didn't cut/print more, it was still promising to keep rates at zero and print as much as it was.

And the promise of “no more” was unbelievable. If pushed the ECB *would* cut and print more.

So prepare for more of the volatile year we've already seen. And then there's our politics.

ANDREW EDDY

MORGANS FINANCIAL

BUY

AMP (AMP) \$5.68

Earnings momentum should continue with strong fund inflows improving equity markets.

BURSON GROUP (BAP) \$4.56

The automotive parts specialist has a clear vision and plan for growth over five years.

HOLD

ORORA (ORA) \$2.48

Has demonstrated solid earnings growth since de-merging from Amcor.

IPH (IPH) \$7.08

The IP services firm with dominant market positions looks likely to make further bolt-on acquisitions.

SELL

AURIZON (AZJ) \$4.02

Facing earnings pressures from cost escalation and customer cost-cutting initiatives due to weak coal markets.

SUPER RETAIL (SUL) \$8.64

Recent result was disappointing and highlighted difficult trading conditions for the Leisure division.